Course Evaluation, Summary and Conclusions

Final Exam

- Saturday, December 20th
- 12:30 – 3:30 p.m.
- 230 Hearst Gym

Agenda

- Course Evaluation
- Summary
  - The IS-LM, DAD-SAS, and SGM together.
  - Macroeconomic Rules of Thumb.
- Conclusions

Course Evaluation
Summary

• Three models of economic activity:
  - The IS-LM model.
  - The DAD-SRAS model.
  - The Solow Growth model.

Summary

• The IS-LM Model:
  - Short-run orientation.
  - Determination of Y and r.
  - Prices are exogenous.
  - Y can deviate from Y* in the short-run.
  - Adjustment mechanism is through inventory change and changes in r.

Summary

• The DAD-SAS Model:
  - Medium-run orientation.
  - Determination of Y and \( \pi \).
  - Wage and price adjustment is sticky.
  - Y can deviate from Y* in the short-run but not in the intermediate-run.
  - Adjustment mechanism is through \( \pi \), changes in the real Ms, and r.

Summary

• The Solow Growth Model:
  - Long-run orientation.
  - Determination of \( Y*/N \), Y*, and \( y\)-dot.
  - Wages and prices are fully flexible.
  - Y does not deviate from Y* in the long run.
  - Adjustment mechanism is through adjustments in investment-per-worker and the capital-to-labor ratio.
Summary

- The IS-LM, DAD-SAS, and SGM are fully consistent with one another.
  - Changes in one model **MUST** be transmitted to the other models in a fully consistent manner.

Changes in fiscal policy

Changes in monetary policy

Changes in productivity
Macroeconomic Rules of Thumb

- Based on Okun’s Law and the DAD – SAS Model (with only demand shocks).

Macroeconomic Rules of Thumb

- Economic output:
  - If the output ratio \( \frac{Y}{Y^*} \) is rising,
    \[ \frac{\Delta Y}{Y} > \frac{\Delta Y^*}{Y^*}. \]
  - If the output ratio \( \frac{Y}{Y^*} \) is falling,
    \[ \frac{\Delta Y}{Y} < \frac{\Delta Y^*}{Y^*}. \]

Macroeconomic Rules of Thumb

- Economic output and unemployment:
  - If \( Y > Y^* \), then \( U < U^* \).
  - If \( Y < Y^* \), then \( U > U^* \).

Macroeconomic Rules of Thumb

- Implications:
  - If \( \frac{Y}{Y^*} \) is rising, then \( U \) is falling.
  - If \( \frac{Y}{Y^*} \) is falling, then \( U \) is rising.

- Conclusion:
  - Changes in the unemployment rate depend on changes in the output ratio, NOT on its level.
### Macroeconomic Rules of Thumb

**Implications:**
- If U is falling, then Y/Y* is rising.
- If U is rising, then Y/Y* is falling.

**Conclusion:**
- Changes in the output ratio depend on changes in the unemployment rate, **NOT** on its level.

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**Implications:**
- Economic output, unemployment, & inflation:
  - The relationship between economic output and inflation is more subtle than the relationship between economic output and unemployment.
  - It depends on whether the economic output is above or below its full-employment level.
    - That is, whether the output ratio (Y/Y*) is > or < 1.

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Conclusions about Macroeconomics

- Conclusions about Macroeconomics:
  - What we know.
  - Questions searching for better answers.

Conclusions about Macroeconomics

- What We Know:
  - *In the long-run*, a country’s standard of living is determined by its capacity to produce.
  - *In the short-run*, changes in aggregate demand influence a country’s production.

Conclusions about Macroeconomics

- Questions Searching for Better Answers:
  - Exactly how should a country go about attempting to raise its standard of living?
  - What are the best institutions for achieving economics goals?
  - How and should policymakers try to stabilize the economy?
Conclusions about Macroeconomic

• Questions Searching for Better Answers:
  ➢ How do we measure full-employment output in practice?
  ➢ Exactly how costly is inflation and how costly is it to reduce inflation?
  ➢ How big a problem are substantial budget and/or trade imbalances?

For Exam #3

• Coverage: Chapters 9, 12 & 13.

• Format:
  ➢ 10 multiple choice questions.
  ➢ 1 long question on Inflation.
  ➢ 1 long question on International Economics.

For Exam #3

• Date: Saturday, December 20th
• Location: 230 Hearst Gym
• Time: 12:30 p.m. – 3:30 p.m.
  ➢ Exam will start as close to 12:30 p.m. as possible.
  ➢ The exam will end promptly at 3:30 p.m.

For Exam #3

• Exam Packet is completely self-contained.
  ➢ No blue books are needed.

• No books, notes, or electronic devices.
  ➢ Foreign language dictionaries MUST be examined by me before the exam begins.
For Exam #3

- You will need a set of colored pens or pencils.
  - Black or pencil.
  - Red
  - Blue
  - Green

See you in 11 days!

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